

Revenue Review

Tennessee Department of Revenue

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REVENUE ...
Working For You



April 2005

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Did You Know...

You can receive notices and other publications instantly by signing up on the department's ListServ? Visit our Web site to subscribe to Revenue-News or lists dedicated to county clerks and city officials.

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(800) 342-1003

Streamlined Sales Tax Update

NOTE: The Governor has requested that the department review the Streamlined Sales Tax legislation to determine whether the law or parts of the law should be altered or delayed. **As of the printing date of this newsletter, this evaluation is still in progress.** Any changes will be posted on our Web site, as well as on our call center line.

The department has been preparing for July 1, 2005, the effective date of the Streamlined Sales and Use Tax conforming legislation. These changes include some of the most comprehensive tax changes since the adoption of our sales tax laws in 1947.

In 2003, the department was asked by legislators to draft legislation that would conform Tennessee's sales and use tax statutes to the provisions of the Streamlined Sales and Use Tax Agreement. Many meetings were held with groups representing various business and government interests in order to explain the changes and policy choices that would be required in order for Tennessee to be a Streamlined Sales Tax state. Those efforts resulted in passage of Public Chapter 357 Acts of 2003 and the subsequent technical correction legislation, Public Chapter 959 Acts of 2004.

The Streamlined Sales and Use Tax Agreement is the product of a multi-state effort to simplify and make more uniform sales tax laws across the country. Currently, 42 states and the District of Columbia participate in this effort. At this time, 21 states have changed their laws to align them in whole or in part with the Streamlined Agreement.

The goal of the Agreement is to make laws simple or uniform enough so that all sellers making taxable sales into Tennessee will collect Tennessee sales tax from their purchaser. Currently, only sellers with a physical presence in Tennessee are required to collect our sales taxes. While businesses and consumers have a legal obligation to self-report and pay use tax on items brought into Tennessee where no sales tax has been collected, many do not. This is a major area of noncompliance with Tennessee tax laws and it is one that could be much more efficiently addressed by having all sellers collect the tax. Furthermore, Tennessee and other states are concerned over the growth in sales through electronic commerce and catalogs. If these remote vendors do not collect our sales tax, there is a loss in revenue to state and local governments and an economic disadvantage to local merchants who are required to collect our tax.

Information about the Streamlined Agreement is available on the department's Web site and through a special hot line and e-mail address. A comprehensive PowerPoint

presentation that reviews law changes for Tennessee has recently been added to the department's Web site. Taxpayer education efforts have included more than 70 presentations across the state by trained staff members. Currently, the department is in the process of scheduling and making industry-specific presentations throughout Tennessee.

The department will be posting and mailing important notices to taxpayers, as well as revising existing sales and use tax rules. We hope to file these rules with the Secretary of State to begin the promulgation process in the spring of 2005. The Sales and Use Tax Guide will be updated to incorporate Streamlined changes by June.

Generally, the Streamlined Agreement requires states to adopt simplified rate and tax base structures, use uniform definitions, simplify the manner in which exemptions are handled - including the use of a uniform exemption certificate, remove the use of caps and thresholds in its laws, and to adopt many other changes.

The most widely-discussed aspect of the Streamlined law changes is the change to "destination sourcing." In an effort to make laws uniform, the states were required to agree on one rule with regard to where a sale was sourced so that a seller could decide whose tax to collect. Tennessee "sourced" all sales to where a business was located. If a sale was being shipped out of state, the seller did not collect Tennessee sales tax. The "situs" or "origin" based rule of sourcing that Tennessee uses creates opportunities for "tax-rate shopping" and presents numerous other administrative problems. The states chose to adopt the rule of "destination sourcing" which generally will work as follows: If a customer takes possession of an item at the location of a store, the seller collects the rate of tax for the jurisdiction in which the store is located. If a customer has the item delivered to another jurisdiction, the seller collects the rate of tax for the jurisdiction to which the good is delivered.

This is a major change for Tennessee businesses that make delivery sales into different cities and counties. The department has created a tax rate and jurisdictional boundary database to assist in this change. An online version of the database that allows taxpayers to type in a street address, city and zip code and obtain the tax rate and local tax jurisdiction is available on our Web site. A downloadable flat file version of the database designed to integrate with different software is projected to be available in April 2005. The department also plans to implement a voice-activated system that will be available 24 hours a day, seven days a week, and will allow taxpayers to call in toll-free and obtain the tax rate and local jurisdiction for an address. A paper form of the

rates and jurisdictional database will be available to taxpayers who do not use computers in their business.

Given the scope of this change, Commissioner Chumley has announced a grace period of six months following July 1, 2005, in order for businesses to make the change to destination sourcing.

Our employees understand the difficulty that comes with change, and it is our goal to have tools and resources available to taxpayers to assist in making the Streamlined changes. You have our commitment to work with you to make the implementation of these law changes as smooth as possible.

Tennessee Individual Income Tax

Tennessee's individual income tax applies to certain forms of interest and dividend income. Individuals, trusts, partnerships and other entities receiving interest from bonds and notes and dividends from stock are liable for the Tennessee income tax. Interest income from bank savings accounts, certificates of deposit and Tennessee municipal bonds is exempt. Interest from non-Tennessee municipal bonds and long-term notes is taxable. Dividends from stock, including ordinary dividends and capital gain distributions from mutual funds, are taxable. The tax rate is 6% of taxable income. The first \$1,250 in taxable income received by a single filer is exempt. The first \$2,500 in taxable income received by a joint filer is exempt. People over 65 with total income less than \$16,200 for a single filer or \$27,000 for a joint filer are exempt. More information is available on the department's Web site, www.Tennessee.gov/revenue.

Frequently Asked Individual Income Tax Questions

Why must I list my county and city on the return?

The income tax collected is shared with the cities and counties. Five-eighths of the revenue collected is deposited into the general fund. The remaining three-eighths is distributed to the cities and counties.

If the taxpayer resides within the corporate limits of a municipality, three-eighths is distributed to the city. If the taxpayer does not reside within a municipality, the revenue is shared with the county.

If I request an extension of time to file and later discover I do not owe any tax, must I file a return?

No, a return is not required if no tax is due. However, if an estimated payment was submitted with the extension request, a return must be filed to request a refund.

My 1099-DIV lists a part of the dividends paid under a box labeled "nontaxable." Does this mean the income is not taxable to Tennessee?

No. The 1099-DIV form is a federal tax form, and dividends paid are reported on the form based on federal tax law. Tennessee income tax differs from federal tax in many aspects. In most instances, the dividend still will be taxable to the Tennessee resident, unless a specific exemption exists in Tennessee law.

My partnership files a franchise and excise tax return. Must I also file an income tax return?

Yes, if the partnership has taxable interest and dividend income above the exemption, an income tax return must be filed. Credit for any income tax paid may be claimed against the excise tax on Schedule D of the franchise and excise tax return.

File Individual Income Tax Online This Year


Tax season is in full swing, and the April 15 deadline is fast approaching. The Tennessee Department of Revenue reminds individual income tax filers that online filing of this tax, commonly known as the Hall income tax, is available on its Web site, www.Tennessee.gov/revenue. Like Revenue's other electronic applications, this option is a convenient, worry-free tax filing service that performs some or all calculations for filers.

The Department of Revenue reminds all individual income tax filers that they still must file a federal extension or an extension with the department in order to obtain an extension that will be accepted by the department.

Franchise and Excise Tax Reminder

Normal franchise and excise returns are due April 15. Effective for tax years beginning on or after Jan. 1, 2004, a taxpayer that is a member of an affiliated group or a financial institution affiliated group may elect to compute its franchise tax net-worth base on a consolidated basis.

Those taxpayers making the election will be required to file a group registration form with the department and provide all information necessary to establish the affiliated group or financial institution affiliated group on or before the due date of the tax return for the period for which the election is to take effect.



You may owe gift tax if you:

- Quitclaim property to someone, such as a child
- Transfer property to someone for less than the fair market value

Questions? Need more information? Call (615) 532-6438.

Are you a registered taxpayer? If YES, we need your tax contact's e-mail address, so we can e-mail information in the future. Call toll-free (800) 342-1003; Nashville-area and out-of-state callers, dial (615) 253-0600.

Compliance Information for On-premise Retailers of Alcoholic Beverages

- Persons licensed by the Alcoholic Beverage Commission to sell alcoholic beverages for consumption on the premises must remit a 15% gross receipts tax (liquor-by-the-drink tax) as well as sales tax on total monthly sales. (Tenn. Code Ann. Section 57-4-301)
- Alcoholic beverages subject to this tax include liquor and wine but not beer.
- Unlicensed persons selling mixed drinks and/or setups for mixed drinks are liable for a 15% gross receipts tax (mixing bar tax) as well as sales tax on total monthly sales. (Tenn. Code Ann. Section 67-4-410)
- Admission fees or "cover charges" collected by a bar or restaurant are not subject to liquor-by-the-drink tax or mixing bar tax but are taxable amusement admission charges for sales and use tax. (Tenn. Code Ann. Section 67-6-212(a)(2)). Admission or cover charges to parties or events at a taxpayer's business are subject to sales/use tax on amusements. Specifically, Tenn. Code Ann. Section 67-6-212(a)(2) levies tax on "sales of tickets, fees or other charges made for admission to or voluntary contributions made to places of amusement, sports, entertainment, exhibition, display or other recreational events or activities."

Price Schedule

- Each licensed retailer of alcoholic beverages is required to file a price schedule, available on Revenue's Web site at this link, <http://state.tn.us/revenue/forms/liquorbydrink/f1301101.pdf>. This is a schedule of the retailer's most commonly sold alcoholic beverage drinks. The licensed retailer must provide accurate information on the price schedule and keep the schedule current. **This form serves as the basis for every liquor-by-the-drink audit.**
- The price schedule must be filed prior to entering business and again when any change is made in any information contained on the price schedule. Revised schedules should be filed with the department prior to the effective date of change.
- In Tennessee, a licensee can only make distributions of alcoholic beverages through sales for consumption on the premises. Consequently, the average markup on alcoholic beverages indicated by the books and records of a licensee should closely approximate the average markup of the price schedule filed with the department. For example, if all drinks are sold for \$5 and the alcohol cost for each drink is \$1, then your average markup is five times cost or 500%. If your alcohol purchases for a month were \$2,000, then we would expect your reported sales to be approximately \$10,000 (500% x \$2,000 cost).

Purchase Markup Audit

- If the average markup as shown by the books of a licensee does not closely approximate the average markup as shown

by the price schedule, the department will consider the books of the licensee insufficient to show the proper tax liability.

For this reason, the department will calculate the licensee's correct liability using the purchase markup method.

- The procedure for a "purchase markup" audit begins with a tax auditor making a determination as to what the inventory of the business was as of the last day of the audit period. When a beginning inventory has been established, the auditor will add to the beginning inventory all purchases made during the audit period using all available records. The ending inventory then will be subtracted from this figure to arrive at the cost of goods sold during the audit period. The average markup as reflected by the price schedule(s) will then be multiplied by the cost of goods sold during the audit period to arrive at the dollar amount of alcoholic beverages sold during the audit period. After sales are determined in this manner, the tax rate will be applied to the sales figure, and tax payments made during the audit period will be subtracted to arrive at any additional tax liability. As can be seen, it is very important for the licensee to maintain proper records in order to show proper reporting of alcoholic beverage sales over the audit period.

More information on the tax obligations of retailers of alcoholic beverages may be found on our Web site, www.Tennessee.gov/revenue.

Ongoing Compliance Efforts: Use Tax

Many Tennessee businesses and consumers are unaware that use tax is owed on items they have imported into this state without paying sales tax to the seller. Use tax applies to the same merchandise taxable under Tennessee's sales tax laws. Examples of items subject to use tax include, but are not limited to, the following: furniture, collectibles, art work, airplanes, televisions, clothing, video equipment, jewelry, computers, appliances, stereos, cameras, furs, and books. If you purchase anything from out of state and the seller fails to collect tax from you, you must file and pay use tax at the rate applicable to your business or home (7% state tax plus the local rate of your address).

In order to identify merchandise imported into Tennessee without the payment of sales tax, the department actively participates in various information exchange programs with other states, and with federal agencies, such as U.S. Customs and the Federal Aviation Administration. Using this information, the department contacts purchasers about their use tax obligations.

Additional information about use tax is available on the Web site, www.Tennessee.gov/revenue.

Are you a registered taxpayer? If YES, we need your tax contact's e-mail address, so we can e-mail information in the future. Call toll-free (800) 342-1003; Nashville-area and out-of-state callers, dial (615) 253-0600.

Save the Date: Upcoming Seminars and New Business Workshops Across the State

Visit our Web site, www.Tennessee.gov/revenue, and click on "Seminars, New Business Workshops and Speakers" to learn more about these and other upcoming seminars and workshops.

May

- May 11** – New Business Workshop, Chattanooga
- May 12** – New Business Workshop, Johnson City
- May 12** – New Business Workshop, Memphis
- May 18** – New Business Workshop, Knoxville
- May 24** – New Business Workshop, Nashville

July

- July 13** – New Business Workshop, Chattanooga
- July 13** – New Business Workshop, Knoxville
- July 13** – Tennessee Business Taxes, Austin Peay State University, Clarksville
- July 14** – New Business Workshop, Johnson City
- July 14** – New Business Workshop, Memphis
- July 14** – Tennessee Business Tax, University of Tennessee, Knoxville
- July 21** – Tennessee Business Tax, Middle Tennessee State University, Murfreesboro
- July 26** – New Business Workshop, Nashville
- July 27** – Tennessee Business Taxes, The Centre at Millennium Park (East Tennessee State University), Johnson City
- July 29** – Tennessee Business Taxes, University of Memphis, Memphis

Registration Reminder for Tennessee Retailers

When a business is started or a new location is added, the owner must register the business location with the department. The easiest way to apply for a certificate of registration is to register online at <http://www.tennesseeanytime.org/bizreg/>. Registrants may also visit one of the Department of Revenue's offices. Trained personnel are available to explain Tennessee's tax system and to answer questions.

Whether registering online, in person, or by mail, registrants must have the following information to complete a application:

- The name, address, and phone number of the business, all owners, officers, or partners, and the person making the application.
- The Social Security number(s) of the owner(s), partners or officers.
- The Federal Employer Identification Number (FEIN) issued by the Internal Revenue Service if he/she has one.
- A description of the business, the type of ownership, a brief explanation of the nature of the business, and, if the business is a corporation, the date of incorporation.
- The name and address of the previous owner, if he/she has purchased the business.
- The signature, on the application, of the sole proprietor, a partner, or an officer of a corporation.



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January Collections

January 2005 collections of the Tennessee Department of Revenue were \$929,321,408, an increase of \$73,504,381 or 8.6 percent over January 2004 collections. Sales and use tax collections were \$620,404,640, up \$35,326,209 or 6 percent over January 2004 collections. Consumer use tax collections were up 21.2 percent from collections in the same period last year. Franchise and excise tax collections were \$149,516,444, up \$28,547,367 or 23.6 percent when compared to January 2004 collections. Collections from the privilege taxes were \$21,753,294, an increase of \$1,252,917 or 6.1 percent over collections in the same period one year ago.

Contact Us

- Taxpayer hot line: Statewide toll-free (800) 342-1003; Nashville-area and out-of-state callers should call (615) 253-0600.
- Online tax help by e-mailing TN.Revenue@state.tn.us.
- Streamlined Sales Tax hot line: In Tennessee, call (877) 250-2299. In Nashville and outside Tennessee, call (615) 253-0752.
- Streamlined Sales Tax online assistance by e-mailing Streamlined.Salestax.QandA@state.tn.us.
- Tax practitioner hot line: Statewide toll-free (800) 387-8395; Nashville-area and out-of-state callers should call (615) 253-0700.
- Local government hot line: (866) 562-2549.
- E-mail updates: Visit our Web site, www.Tennessee.gov/revenue, to subscribe to Revenue-News or lists dedicated to county clerks and city officials.
- Electronic commerce hot line: Statewide toll-free: (866) 368-6374. Nashville-area and out-of-state callers should dial (615) 253-0704.
- Tax fraud hot line: To report tax fraud, call (800) FRAUDTX (372-8389).

Online Sales Tax Filing Statistics

Month	Number of Returns	Total of Amount Collected
November 2004	11,047	\$117,648,643
December 2004	11,440	\$114,063,234
January 2005	13,017	\$134,025,988

We Want Your Feedback

We work each day to serve our customers. Your feedback on our customer service and our Web site helps us provide outstanding service and meaningful, useful information on the Internet. To let us know how we're doing and how we can better meet your needs, visit our Web site, www.Tennessee.gov/revenue. Separate surveys related to our service and our Web site are available for online completion.